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PRINCIPLES AND PROCEDURE
FOR ORGANIZING
COOPERATIVE COTTON GINS

By
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PRINCIPLES AND PROCEDURE
FOR ORGANIZING
COOPERATIVE COTTON GINS

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PURPOSE

Proper organization of a cooperative requires the services of a competent attorney in drafting and adopting the organization papers and in other legal matters, but several important preliminary steps must be taken before the organization is ready to be incorporated. Frequently it is necessary to explain the underlying principles of a cooperative organization to some of the prospective members. Local conditions must be analyzed to determine the need for a cooperative gin, and to consider the possibilities for its success.

The idea of starting a local cooperative gin usually originates with some one individual, or at most with three or four. The task of starting and completing the organization, in most cases, must be done or at least supervised by a small group. It is the general purpose of this publication to provide information and suggestions that will help this group to decide whether or not a cooperative gin is needed in their community and, if it is needed, to assist them in completing the organization.

The more specific purposes of this circular are: (1) to outline some of the desirable features of a cooperative gin; (2) to discuss some of the local factors that are important in determining whether or not a cooperative is needed; (3) to discuss the financial structure and dividend policy; (4) to outline the steps of organization procedure; and (5) to suggest some general forms as a guide to the preparation of the organization papers.

Note. - Acknowledgment is made of the assistance of L. S. Hulbert, Assistant General Counsel, and E. Marks, Assistant Attorney, Farm Credit Administration, in drafting the suggested organization forms included in this publication.

SOME DESIRABLE FEATURES OF A COOPERATIVE GIN

The underlying characteristics of a cooperative gin are quite similar to those of a gin owned by an individual cotton producer and used to gin his own cotton exclusively. In both types, ginning may be considered a part of the production of cotton. Most of the questions regarding the ownership or operation of a cooperative gin may be answered by making comparisons with those of a gin exclusively owned and operated by one cotton producer.

Although the practices of cooperative cotton gins are necessarily modified by the local conditions under which they operate, some features which have been found desirable generally may be stated as follows: 1/

1. Owned by cotton producers who are patrons.
2. Controlled by members.
3. Operated for the benefit of patrons.
4. Charges and prices conservative.
5. Dividends or invested capital limited.
6. Patronage dividends paid.

The cooperative marketing statutes of the various States provide the legal basis for the realization of these cooperative principles.

Owned by Cotton Producers Who are Patrons

Ownership of a gin plant requires an investment of capital. Essentially all the capital of a cooperative gin should eventually be supplied by the members and patrons if it is to continue to operate successfully. Although a part of the original capital requirements may be borrowed, the initial investment of the members should be sufficiently large to enable the cooperative to assume the ordinary business risks of the venture. Since the liability of an individual member does not exceed the amount of his paid-in and subscribed capital, the combined investment of all the members should be sufficiently large to insure protection to creditors and to each other. From the standpoint of the members themselves, a substantial investment of capital indicates interest in the undertaking and tends to insure loyalty.

1/ Christensen, C. L., Hobson, Asher, Bakken, H. H., Froker, R. K., and Schaars, M. A. Cooperation, principles and practices. Wis. Univ. Ext. Ser. 128 pp., illus. 1936.

The amount of capital originally supplied by each member should preferably be in proportion to his anticipated patronage. Since the benefits of cooperative ginning are in proportion to the use made of the services of the association, the same standard should be followed with respect to the invested capital. In view of the desirability of providing capital in proportion to patronage, a long-time financial program that tends to maintain this relationship year after year is much to be desired. A plan for revolving the capital structure will tend to accomplish this purpose.

Controlled by Members

Control by members is perhaps the most universally recognized principle for cooperative gins. Regardless of how much or how little a member has invested in the capital of the association, he has - with few exceptions - one and only one vote. In most of the cotton-producing states the cooperative statutes make such a practice mandatory. In the few states where other bases of voting are permitted, most cooperatives have elected to follow, or in actual practice do follow, the one-man one-vote principle.

Membership in a cooperative is personal rather than financial. Investments of members in a cooperative gin are made not for the purpose of realizing a return on capital as such, but to provide efficient ginning service at minimum cost. Members of a cooperative gin receive benefits primarily as patrons and not as investors, and therefore, should control the gin because they are patrons rather than investors. 2/

Control by members of the ordinary business operations of a cooperative gin is necessarily indirect. Members control the general policies of the association since they adopt and amend the bylaws under which the association operates. They also elect a board of directors, which, in turn, employs a manager. The manager is responsible for actual operation of the gin. Since all or part of the directors are elected annually, the members are able to exercise considerable control over them. Directors, however, are in contact with the members frequently and are constantly influenced by their views.

Operated for the Benefit of Patrons

Benefits from cooperative gins may be realized in better ginning services as well as in patronage dividends. A cotton producer is interested in the total net value of the lint and seed after all costs of ginning have been paid. If the existing ginning facilities in a community are such that the value of the lint is reduced by

2/ See Robotka, F., and Laughlin, G. C. Cooperative Organization of Iowa Farmers' Creameries. Farm Credit Administration. Bull. 14. 92 pp. illus. 1937.

improper ginning, a well-equipped cooperatively owned gin plant might pay substantial dividends in quality of service, even though the rates charged were higher than those of existing gins.

Benefits cannot always be measured on a short-time or temporary basis. After a cooperative gin is established, consideration should be given to the ginning conditions that might exist in the absence of the cooperative gin. Competing gins may for a time offer lower ginning charges than actual operating expenses justify, or pay higher prices for cottonseed and other products than the market warrants. The purpose of such practices may be either to force the cooperative to do likewise, or to attract the patronage of the members if the cooperative refuses to do likewise. If the members of the cooperative gin are so shortsighted as to permit either of these results the cooperative may fail. Then charges and prices that are profitable to the commercial gins will be reestablished.

Charges and Prices Conservative

As a rule cooperative gins charge for ginning and wrapping and pay for cottonseed and other products at the same rates that prevail at nearby commercial gins. In numerous instances, however, the cooperative gin has refused to become involved in rate cutting and price wars, but has charged a higher rate for ginning and paid a lower initial price for cottonseed and other products than competing commercial gins. A cooperative gin whose capital and patronage are derived from its members cannot hope to do more or less in the final analysis than to render ginning services at actual cost, and pay resale price less handling costs for cottonseed and other products handled. 3/

When the initial charges for ginning and wrapping are higher than the total cost of providing these services, and the prices paid or advanced for cottonseed and cotton are below the net prices for which these products can be resold, a net income will result. If this income is then distributed in proportion to the business contributed, the member will in the end pay actual cost for ginning and wrapping and receive the resale price less handling costs for cottonseed and cotton.

On the other hand, if the cooperative charges its patrons, who also furnish its capital, lower rates for ginning and wrapping than the cost of performing these services and pays more for cottonseed and cotton than the prices at which these products can be sold, a loss will be sustained. This loss will necessarily reduce the net worth of the association. Any impairment of the invested net worth of the group will in turn offset the apparent gain from low ginning

3/ Paulson, W. E. Some problems in the successful operations of cooperative cotton gins. In the Southern Social Science Quarterly, v. 28. June 1937.

rates and excessively high prices for products. The net result is again that the final charge for ginning will be its cost, and the final price for cottonseed will be the resale price less the cost of handling. If an association has patrons who are not stockholders, any losses resulting from overpayment or inadequate charges will be at the expense of the stockholders and to the benefit of nonstockholders.

Regardless of the policy followed with respect to rates and prices, the members of a cooperative gin - who furnish both the capital and the patronage - cannot do more or less than obtain these services at cost. The members can no more make a profit on their own business as such than an individual farmer, owning and operating a gin plant to handle his own cotton exclusively, could make a profit by charging himself very low ginning rates and paying himself very high prices for cottonseed and cotton.

The rates and prices established by a cooperative gin association should be such as to avoid losses from price changes and other normal business risks. By this means the members share these necessary risks in proportion to their patronage just as they share the benefits from cooperation. Another advantage of a conservative policy with respect to initial charges and prices is the possibility of paying substantial patronage dividends at the end of each season. Patronage dividends in relation to initial charges and prices emphasize the benefits of a cooperative gin to its patrons.

Dividends on Invested Capital Limited

Limitation of dividends on invested capital is one of the basic principles of cooperatives. It has stood the test of time and experience since first adopted by the original Rochdale pioneers nearly a century ago.

The legal basis for limiting returns on capital is definitely established. The cooperative statutes of every State place a limit of 8 percent or less on capital dividends. The Capper-Volstead Act, a Federal statute applicable to cooperatives that do interstate or foreign business, provides that a farmer cooperative in order to obtain the benefits thereof must either limit dividends on capital to 8 percent, or limit each member to one vote regardless of the number of shares of stock owned. One of the primary requirements for exemption from Federal income taxes is that dividends on capital stock shall not exceed 8 percent per annum.

State and Federal laws specify only the maximum return that may be paid on invested capital. Cooperative associations may provide for lower rates. The general tendency during recent years among cooperative gins has been to lower materially the returns on capital.

Many associations have limited dividends on stock to 6 percent; others have placed the limit at 4 percent, and quite a few have entirely eliminated dividends on invested capital.

Patronage Dividends Paid

Patronage dividends are the tangible evidence of the financial benefits of a cooperative gin to its patrons. They are the means by which the initial charges for ginning and wrapping are reduced to a cost basis, and the initial prices paid for cottonseed and other products adjusted to the final sales price less handling costs. Since dividends on stock are limited, capital is hired in somewhat the same way as labor, and receives its fixed return before the amount available for a patronage dividend is determined. Any general reserves out of income, such as statutory and educational reserves, and reserves for contingencies, are also set aside before the amount available for distribution as patronage returns is determined. Although patronage dividends come last in the claim on income, they get all that is left. In this respect the amount of patronage contributed to a cooperative corresponds to the amount of common stock invested in a commercial concern.

The ability of a cooperative gin to distribute patronage dividends depends largely on three factors:

1. Adequate volume of business in relation to the size of gin plant.
2. Initial ginning charges sufficiently high to more than cover operating expenses, and initial prices or advances for cottonseed and other products less than prices at which these products may be sold.
3. An efficient and economical operation.

Distribution of income on the basis of patronage is not necessarily limited to cash distributions. If all or part of the net income is used to retire indebtedness, purchase additional facilities, or is used for any other capital purpose, the distribution of patronage dividends may logically be made in additional shares of stock or other certificates, or set up to the credit of the patron's capital account on the books of the association.

When all or part of the net income of a cooperative is used for capital purposes, the patrons in effect make an additional investment in the capital of the association. The amount of this additional investment on the part of each patron is the amount by which the cash patronage dividends of each one would be increased if no part of the income were retained by the association for capital purposes. It is highly desirable that at least part of the net income

be used to accumulate necessary capital, but it is equally desirable that the interest of each patron in this additional investment be recognized and properly evidenced.

Nonmember business is important with respect to patronage dividends. The extent of this business is generally limited by cooperative statutes. It is never legally more than half of the total business. Some State laws altogether prohibit nonmember business; the cooperative statutes of other States permit it if the nonmembers are allowed to share in patronage dividends. In order to obtain exemption from the filing of Federal income tax returns, and the payment of Federal income taxes, it is necessary for a cooperative association to treat nonmembers the same as members with respect to patronage dividends. 4/

If the cooperative features of an association are to be maintained and nonmembers are dealt with at all, a cooperative gin must treat them as members with respect to patronage dividends. It is not necessary that patronage dividends be paid in cash. The payment may be deferred by issuing nonvoting preferred stock or some form of revolving certificates to members and nonmembers alike. If nonmembers are willing and eligible to become members, all of their dividends may first be applied to the purchase of a share of common stock or membership after which they would be treated as all other members. Such a plan with respect to nonmembers offers an excellent means of increasing the membership and volume of the association, thereby perpetuating the existence of the cooperative.

A cooperative gin that does any appreciable amount of nonmember business and does not allow the nonmember to participate in patronage returns, but pays all of the returns to its members, is not strictly a cooperative but rather a profit organization. The members as owners of such an organization become, to a degree, commercial ginnerers. The competitive practices necessary to attract or hold nonmember business will inevitably tend toward those employed by commercial gins.

4/ Knapp, J. G., and Lister, J. H. Cooperative Purchasing of Farm Supplies. Farm Credit Administration. Bull. 1, 92 pp., illus. 1935. See pp. 88-92

SOME ESSENTIAL FACTS TO BE LEARNED BEFORE ORGANIZING

The actual organization of a cooperative gin should not be attempted until a thorough analysis has been made of local conditions affecting its chances for success. Is there a real economic need for a cooperative gin? 5/ Will the members support it by investing capital and contributing patronage? What are the opportunities for economical and efficient operation? These and other pertinent questions should be answered satisfactorily before an organization campaign is begun. An extensive field survey usually is not necessary, as most of these questions can be answered by means of informal discussion among the group originally interested in organization. If there are any active cooperative gin associations within a reasonable distance, it will usually be found helpful to consult with them. County agents and other extension workers of the State Agricultural College as well as the district banks for cooperatives are often able to contribute valuable advice and suggestions.

Some of the important factors to be considered in determining whether or not there is a need and an opportunity for a cooperative gin are:

1. Volume of cotton and number of gins.
2. Reasonableness of existing rates and prices, and quality of service available.
3. Extent and nature of competition.
4. Interest and knowledge of potential members regarding cooperatives.
5. Financial ability and tenure of potential members.
6. Prospect of obtaining competent management, and efficient accounting.
7. Prospect of acquiring an adequate and modern gin plant.

Volume of Cotton and Number of Gins

In analyzing the possibilities for a cooperative gin, it is important to consider the volume of cotton to be ginned in the community in relation to the existing number of gin plants. County figures on bales ginned and number of active gin plants may be had from the annual bulletins of the Bureau of the Census, U. S. Department of Commerce. County figures may be supplemented by local

5/ Sanders, S. D. The Farmers' Cooperative Yardstick. Farm Credit Administration. Circ. 17. 15 pp., illus. 1937.

ginnings during recent years. Although a cooperative gin seldom can expect to handle all of the cotton produced in its territory, the local as well as the county ginnings indicate the maximum possibilities of a local cooperative gin. Certainly the organization should not be contemplated if the total volume available is extremely small.

County ginning figures will also indicate the variation in production from year to year. The production of any given number of members of a cooperative gin may reasonably be expected to vary in much the same degree as the production of the county. Wide variation in production from one year to another makes it difficult to select a gin plant of the most economical size, but the trend of production for several previous years may indicate the production to be expected during the next few years. Since the investment required to purchase a gin plant is relatively large and because the plant is expected to be utilized over a number of years, the possibilities of future cotton production are of equal importance with present production. In this connection special attention should be given to the possible effects of various programs for cotton acreage allotments and control on the future trends in production.

The cotton production per farmer-member and the size of farms within the area where a cooperative gin is contemplated, should be given consideration. Low production per farm means that a relatively large membership will be needed to secure adequate volume. A large membership not only increases the membership and management problems, but also increases the cost of keeping the necessary records. The benefits to a very small producer of belonging to a cooperative gin may not compensate for the necessary investment of capital and the risk involved on his part.

The total number of bales ginned in a county or a local community during any one year, or the production per farm, is of less significance than the average bales per active gin plant. There is, within limits, a minimum volume below which a gin plant of any given size cannot operate economically. Recent studies of cooperative gins have shown that a minimum seasonal volume of at least 500 bales per gin stand is needed for economical operation. Ginning expenses per unit are usually very high if the annual volume is much below 500 bales per gin stand. On this basis a 4-stand plant should have a minimum of 2,000 bales.

Reasonableness of Existing Rates and Prices, and Quality of Service Available

Existing ginning facilities may be adequate, but this does not necessarily mean that a cooperative gin is not needed. The prevailing rates and quality of available ginning services, as well as prices paid for cottonseed or other products, must also be considered. The establishment of a cooperative gin may be justified if the ginning rates charged and prices paid for cottonseed by existing

commercial gins are unreasonable. All of these rates and prices must be considered together in determining whether or not the net result is an equitable charge. For example, the ginning rates and charges for bagging and ties may be very low but the margin on cottonseed excessively high.

It is not easy to analyze the reasonableness of these charges and prices. Much helpful information may be obtained by contacting existing cooperative gins. Some indication of the margin which the local commercial gins are making on cottonseed may be obtained by comparing local prices for cottonseed at the gin with carlot prices at nearby oil mills on the same day. The cost of loading, transportation, and losses from waste and shrinkage should be taken into consideration in making such comparisons.

The most difficult analysis to be made is that of the reasonableness of ginning charges. Studies 6/ of the expenses of cooperative gins in Texas and Oklahoma during 1933-34 have shown that, even with an adequate volume, ginning rates very much below 25 cents per 100 pounds of seed cotton did not allow any considerable income from ginning operations alone. A ginning rate of 25 cents, however, may be either too high or too low for other areas where conditions are different.

A point that often is overlooked in considering ginning rates is that certain operating expenses will be incurred whether the service is performed by a cooperative or a commercial gin. If there is any difference, the cooperative gin will have more expenses. 7/ For example, a cooperative gin will have to keep records much more in detail than a privately owned gin. A cooperative gin frequently spends more for management than a privately owned commercial gin since the commercial ginner may operate a gin as a side line to other business activities.

It is entirely possible that the charges and prices of local commercial gins may be reasonable, and yet an economic need exist for a cooperative gin solely on the grounds that the available ginning services are poor or inadequate. In fact, a poor quality of ginning service may be expected if the prevailing ginning rates are excessively low. To the extent that commercial gins in a given

6/ Paulson, W. E. Costs, Income and Financial Status of Cooperative Gins of Texas, 1933-34. Texas Agr. Exp. Sta. 33 pp. illus. (Mimeographed) 1935.

Weaver, O. T., and Herrmann, O. W. Analysis of the Business Operation of Cooperative Cotton Gins in Oklahoma, 1933-34. Farm Credit Administration. Bull. 12. 96 pp., illus. 1937.

7/ Hulbert, L. S. Organization of Cooperative Associations. Farm Credit Administration. 25 pp., illus. (Mimeographed)

area are furnishing inadequate ginning service and the quality of the ginned lint is damaged, the value of the cotton as reflected in a reduced price may more than offset the low ginning charges.

Extent and Nature of Competition

The local competitive conditions should be carefully considered before starting a cooperative gin. A cooperative gin may be needed either because there is too much or too little competition among existing commercial ginners. Lack of competition is often reflected in high ginning rates and low prices for cottonseed. On the other hand, rate cutting and seed price fights between commercial gins frequently result in poor ginning service and unethical trade practices.

Experiences of numerous cooperative gins have shown that their participation in ginning rate fights and price wars in buying seed or cotton is usually disastrous. A cooperative gin is usually in an unfavorable position to engage in rate and price wars. If any difference exists between the rates and prices between a cooperative and a commercial gin, the cooperative should be on the conservative side and charge higher ginning rates and pay, or rather advance, relatively low initial prices for cottonseed or other products bought.

Even though it were possible for a cooperative gin to charge rates and pay prices to exactly equal the costs of performing these services, such a policy might eventually defeat its purpose since the members might not continue to be aware of the benefits they were obtaining. Competitors would, of course, meet these charges and prices at least for a time, and all cotton producers would tend to benefit equally with the members of the cooperatives at the risk of those who furnished the capital for the cooperative gin.

Interest and Knowledge of Potential Members Regarding Cooperatives

Cooperative gins have been known to have a measure of success without any particular interest in or knowledge of cooperation on the part of the majority of the members. Such cooperative gins were organized where rates and margins were excessively high and, as a result of good business management, the gins have been able to pay substantial patronage dividends year after year. Under less favorable conditions, but equally as great an economic need, such organizations are likely to fail.

Interest in and knowledge of cooperation on the part of the members should be such that temporary price concessions by competitors will not undermine their loyalty. Loyalty must be based on a realization of the long-time benefits of cooperative endeavor. Members must know that the ownership of a cooperative gin plant requires

considerable capital which, in the ordinary course of events, will be furnished by the members; that a cooperative gin has expenses and cannot, over a period of years, do more than furnish ginning services at cost, consideration being given to patronage dividends; and that the maximum price the gin can pay for cottonseed or other products cannot possibly exceed the net price which may be realized from these products. If the members of a cooperative gin are properly informed, the initial charges and prices will not be a matter of primary consideration as all net income above actual cost of ginning and the net earnings on seed will be returned to them as a patronage dividend. Assuming that a cooperative gin is efficiently and honestly operated, the initial charges and prices are of only secondary importance.

Financial Ability and Tenure of Potential Members

The purchasing of a gin plant by a cooperative is nothing more or less than a group of farmers going into the business of ginning their own cotton. This requires an investment of capital on their part. Cooperative cotton gins have been started without the members furnishing any of the initial capital. Such a policy, however, has in many cases proved to be unsound. The interest and loyalty of a member usually is indicated by his willingness to assume some financial responsibility. A considerable amount of actual cash capital is necessary in starting a cooperative gin. A member who is able but unwilling to furnish his part of this capital will likely be among the first to leave the association when any special price inducements are offered by competitors.

Although the ownership of a farm is not an essential qualification for membership in a cooperative gin, a substantial portion of the membership should be reasonably well established and successful farmers in the community where the cooperative is to be located. A farmer who moves from one community to another every year or two is not a good prospect for membership. Membership studies of cooperative associations have shown that established tenants make equally as good members as land owners. 8/

Prospect of Obtaining Competent Management and Efficient Accounting

The lack of competent management is perhaps one of the most serious limitations to the success of cooperative gins. As ginning is seasonal, it is often impractical to offer a competent manager all-year employment. Several cooperative gins, particularly

8/ Jones, J. W. Membership Relations of Cooperative Associations.
Farm Credit Administration. Bull., 2, 1936.

those with a small membership and a small plant, have successfully handled the management problem by hiring a competent head ginner to have complete charge of the mechanical operations of the gin plant and one of the directors or a member, on a seasonal basis and at a small salary, to sell cottonseed and supervise the other business operations of the association. Such an arrangement would likely prove unsatisfactory for a large organization, or one that buys cotton or handles any appreciable side line activities.

An important factor that often is overlooked in analyzing the possibilities of a local cooperative gin is whether or not competent accounting services can be obtained. The weakest part of many cooperative gin associations is the inadequacy of their records. Too often it is assumed that anyone who can write and add can keep books for a gin. This is decidedly not true of a cooperative gin. A record must be kept of the invested capital of each member; likewise a record must be kept of the amount of business contributed by each member to each department of the ginning business. In addition to these detailed individual records, accepted accounting principles ^{9/} and procedure must be followed from the very beginning in recording subscriptions and payments to capital, and in setting up the accounts with fixed assets, if a true financial condition of the association is to be reflected by the books. Likewise, the operating accounts must be accurately kept if an equitable distribution of net income is to be made at the end of each season's operations.

Many cooperative gins have found it desirable to employ a competent public accountant to set up a system of accounting at the beginning of the organization; to supervise it during the active ginning season; and to make an audit of the affairs of the association at the close of the fiscal year. Since much time can be saved by an auditor in checking the records of a system he has installed and supervised, the cost for this extra service is usually more than offset by the savings made in the cost of the audit.

Prospects for Acquiring an Adequate and Modern Gin Plant

Before the organization of a cooperative gin association is started, some information should be obtained with reference to the possibility of acquiring a serviceable gin plant of the proper size. Specifications and prices on new plants may be obtained from gin machinery companies. Tentative prices on local gin plants that can be bought may be obtained from various sources. It is sometimes desirable for a newly organized cooperative to purchase one of the existing local gin plants if it can be bought at a reasonable price. Not only does this lessen the competitive situation, but it allows the local commercial ginner an opportunity to liquidate his

^{9/} Weaver, O. T. Accounting Principles for Cooperative Cotton Gin Associations. Farm Credit Administration. Bull., 2. 92 pp., illus. 1935.

investment. Before final purchase arrangements are made for any used plant, the services of a disinterested gin appraiser should be obtained to determine its mechanical condition and value.

Some cooperative gin organizations have found it desirable to lease rather than buy a gin plant. Such a plan may have some merit in that it permits the association to begin operations with a limited amount of paid-in capital. However, since the actual ownership of a gin plant gives a cooperative much more permanency and stability than a lease arrangement, definite plans should be made to acquire a plant eventually. Sometimes lease for a gin plant may be made with an option to buy. This is much more desirable than an ordinary lease. If an option to buy is obtained, plans should be made to retain all or at least part of the net income while operating under the lease in order to accumulate capital to make the initial payment when that plant or some other plant is purchased.

Buying a complete new gin plant is preferable to either buying or leasing a used plant. New gin machinery is not only more modern and serviceable, but it usually has a very definite psychological advantage in that members will have more pride of ownership and greater confidence in the quality of the ginning service obtained.

FINANCIAL STRUCTURE AND DIVIDEND POLICY

The financial structure and dividend policy of a cooperative are closely related. It is generally considered desirable that members and other patrons furnish the necessary capital in proportion to the use which they make of the services of the association. For that reason the financial structure and dividend policy should be such as to bring about and maintain this proportionate relationship.

Classes of Stock

There are some advantages in dividing the capital of a cooperative into two classes such as common and preferred stock. The object in issuing two kinds of stock is that voting rights may be incident to one, and prior ownership rights in case of sale or liquidation of assets may be incident to the other. The suggested articles of incorporation and bylaws (appendix A) provide for common and preferred stock, but other forms of certificates evidencing control and ownership may be used instead. The following list suggests some of the possible combinations of evidences of control and ownership:

(1) Evidences of control or voting

Common stock
Membership certificates

(2) Evidences of ownership or contributions to capital

Preferred stock
Certificates of interest, equity, or ownership
Individual book credits
Revolving fund certificates

Any one combination of these evidences of control and ownership, if consistent with the State cooperative statute, should serve equally as well as any other combination. The provisions incorporated in the particular share of stock or other certificates adopted are of more importance than the name by which it is called.

certificate

The membership/or voting stock should have a relatively low par value in order that membership may be easily established. A par value of \$10 or even \$5 per share is generally desirable. If the membership stock is limited to one share per member and the par value is low it will not be necessary to pay any dividends on it since the amount invested by each member would be small. Likewise, it will be less difficult for the association to buy in or retire this one share of common stock or membership as soon as a member definitely ceases to patronize the association. This will enable the association to keep the voting control in the hands of its active members and thereby reduce the likelihood of not having a quorum of the members in attendance at annual or special meetings.

The major part of the original capital investment of each member would be evidenced by preferred stock or some other similar non-voting certificate. If preferred stock is used the par value should be low in order to avoid, insofar as possible, the issuance of fractional shares. For this reason a par value of \$1 per share is generally considered preferable to higher values.

Various kinds of certificates such as revolving fund certificates or certificates of interest have certain advantages over preferred stock as a means of evidencing invested capital. In evidencing retains made for capital purposes these certificates may be issued for odd amounts as contrasted to the prescribed par value of stock. In addition, a given series of these certificates may be retired in part by making a pro rate payment on the amount of each certificate of the series, with proper endorsements on the back.

Sources of Capital

There are four general sources from which a cooperative gin may obtain capital: (1) sale of capital stock or membership; (2) borrowing; (3) income from operations; and (4) a specific per unit capital investment by patrons each time a bale of cotton is ginned. 10/

Practically all of the initial capital raised at the time an association is organized is usually obtained by selling stock or memberships to those who become members. Occasionally local merchants or other interested individuals may buy some nonvoting preferred stock. Borrowing is a means of raising temporary capital from lending agencies or individuals other than members. If the association is successful and continues to operate, essentially all of this borrowed capital will eventually be replaced in some manner by an additional investment, on the part of members and other patrons. The use of income to pay off indebtedness or to otherwise build additional capital, means, in effect, that the patrons are making an additional investment in the capital of the association since the income of a cooperative belongs to its patrons. Even when the interest of each patron in this increased equity in the association is not recognized by the payment of patronage dividends in credits on additional stock, other certificates, or book credits, this income becomes undivided surplus and as such is a part of the capital of the association.

It is, of course, preferable that such capital be evidenced by shares of stock, other certificates, or book credits, each year during the time that any net income is used for capital purposes. Unless this is done the patrons who contribute the business during those years will not receive equitable treatment with respect to distribution of net income and their actual investment in the capital of the association.

10/ For a more thorough discussion of this means of providing capital, known as the revolving capital plan, see: Sanders, S. D., Organizing a Farmers' Cooperative, Farm Credit Administration Circular No. C-108, 42 pp. 1938. pp. 7-10.

The fourth source of capital, that of a specific per unit charge for capital purposes, has not been generally accepted by cooperative gins. It is an excellent means of providing capital that might well be given serious consideration by associations interested in adopting a sound and orderly plan of financing. Such a plan provides that each patron will make a small investment in the capital of the association each time he gins a bale of cotton. This per unit investment may be, for example, 5 cents per 100 pounds of seed cotton ginned, \$1 per bale, or \$2 per ton of seed. Although this payment for capital would be in addition to the regular charge for ginning and wrapping, it is definitely not an expense or cost to the patron but a recurring investment on his part in the capital of the association each time he uses its service.

At the end of each fiscal year each patron would be issued preferred stock, or some other similar certificate, for the total amount of these per unit payments for capital made that year, together with his part of any net income retained for capital purposes and not distributed as cash patronage dividends. This plan of financing has been successfully used by some of the cooperative gins that have recently been organized in California.

Such a plan of financing is especially desirable for a new association that has to borrow a considerable part of the capital required to buy a gin plant, in that it provides a reasonably certain source of capital funds to liquidate the indebtedness, and thereby makes it much easier for the association to obtain a facility loan, especially from the banks for cooperatives.

Revolving the Preferred Stock or Other Certificates

As soon as an adequate amount of capital had been accumulated by these means, and essentially all of the indebtedness of the association paid off, the amount of funds arising each year from these per unit capital contributions and retained earnings would be used to retire an equal amount of oldest outstanding or first issued preferred stock. Under such a plan the capital of the association would be revolved among the active patrons from year to year, and each patron in time would acquire capital approximately in proportion to his patronage. New members would gradually contribute their part of the capital as they continued to patronize the association.

Should a member withdraw, or for any other reason cease to patronize the association, it would not be necessary or desirable for the association to immediately buy in his preferred stock, or other similar certificates used. A part of this stock would be retired year by year in the same order and manner as if he continued to patronize the association. When a patron has acquired his proportional part of the capital through such retains, this proportion will tend to be maintained as the patron will then begin to receive additional cash returns from the retirement of his stock.

Total Amount of Original Capital Needed

The total amount of original capital which will be required by a newly organized cooperative gin depends largely on the cost of the gin plant which is to be purchased. An investment of \$10,000 or more usually is needed to buy even a second-hand plant that is in a serviceable condition; new plants may cost more than twice that amount depending on the size, type of power, and amount of extra equipment desired.

Capital Originally Furnished by Members

The members as a group should subscribe for at least 40 percent of the cost of the gin plant. As much as possible of this amount should be paid in cash, with bona fide stock subscription notes executed in favor of the association for the balance.

Insofar as it is possible the original investment of each member should be in proportion to the volume of business which he expects to furnish. For example, if the initial capital to be raised by members is \$10,000 and the association expects to gin an average of 2,000 bales, it would be desirable for each member to purchase \$5 of preferred stock for each bale to be ginned in addition to the one share of common stock. This proportionate investment on the part of members and patrons may be maintained year after year by the use of a revolving plan of financing.

Borrowed Capital

Most cooperative gins usually borrow half or more of the original capital needed to purchase a gin plant. Such loans are obtained from various sources including banks for cooperatives, commercial banks, gin-machinery companies, cottonseed oil mills, former owners of gins, and other sources, and are generally secured by a first mortgage on the gin plant.

In the purchase of physical facilities such as gin plants the district banks for cooperatives are authorized to lend cooperative associations up to 60 percent of the value of these facilities. 11/

11/ Sec. 7 of the Agricultural Marketing Act as amended (U.S.C. Title 12, Sec. 1141 E.)

These loans are usually amortized over a period of 5 to 10 years. One of these banks for cooperatives is located in each farm credit district at the same address as the Federal land bank.

Accurately Determining Net Income

The accurate determination of net income becomes increasingly important if a revolving plan of financing is used. If the actual net income as shown by the operating statement is consistently overstated year after year and additional shares of stock or other certificates distributed on that basis, the association is in effect "watering" its stock as the face value of these capital items will eventually far exceed the net assets of the association. Likewise, the payment of cash patronage dividends in excess of the actual net income, regardless of whether or not a revolving plan of financing is used, will eventually result in an impairment of the stated capital of the association.

Net income from operations is sometimes confused with the amount of cash on hand at the end of the year. A cash balance on hand does not necessarily indicate that a net income has been made; neither does the absence of a cash balance necessarily mean that a loss has been sustained. A net income from operations results only when the association has charged its patrons more for the services it has rendered than the total cost incurred in performing these services. Each year's net income is determined by deducting from gross income all cash expenses already paid as well as certain other accrued and estimated expenses that will not be paid until later but which have already been incurred, and by adding all expenses prepaid at the end of the fiscal year.

Interest and taxes, for example, that are accrued at the end of a fiscal year, even though not yet due, are just as much a part of that year's expenses as if already paid. Likewise, the cost of repairs necessary to restore the gin machinery and other physical facilities to a reasonable operating condition are chargeable to the current year's operations rather than the following year. On the other hand, the unused portion of insurance and bond premiums already paid before the close of the fiscal year is chargeable to the following year's operations rather than the current year. Depreciation on buildings and machinery, though not represented by a cash outlay, is nevertheless an expense of operation each year. Depreciation has been defined as "an allowance to meet losses (expenses) already incurred in fact, but indefinite in amount." A gin plant will eventually wear out completely, or at least become too obsolete for economical use. The entire cost of replacing the plant in whole or in part should not be considered an expense in the year in which the replacement happens to be made. The expense involved belongs to the operations of each of the years during which the plant was being worn out. Depreciation is a means of charging a part of the cost of these replacements to the expenses of each year's operations, and thereby building up reserves by retaining assets in the business

to pay for the replacements as they become necessary. When the replacements are eventually made, the cost is not an expense of that year's operation but merely reduces the reserve previously accumulated and set up for that purpose.

Income by Departments

The income from each department of the ginning business should be determined separately in arriving at the total net income. This is desirable not only for intelligent management of the business during operation, but also to provide for an equitable distribution of patronage returns at the end of each fiscal year.

Consideration should be given to the items of expense that are to be charged against each of the departments in arriving at income. All direct expenses would, of course, be charged against the department for which incurred. Since ginning and wrapping are the primary activities of a cotton gin, it is generally considered preferable to charge all overhead expenses such as management, office expense, advertising, and interest on indebtedness to this department. However, a portion of some of these expenses may logically be prorated between the different departments on some equitable basis.

Distribution of Net Income

The policy of a cooperative with respect to the distribution of net income should be financially sound from the standpoint of the association and equitable from the standpoint of those entitled to receive dividends. In order to accomplish these objectives it is suggested that all of the net income be allocated each year in the following order and manner:

- (1) At least 10 percent to a general reserve.
- (2) A dividend of not to exceed 8 percent on fully paid capital.
- (3) The balance on the basis of patronage.

The allocation of a portion of net income to a general reserve does not mean that actual cash funds must be set aside. The use of such a reserve merely withholds a part of each year's income from distribution as dividends and thereby increases the capital of the association by retaining assets in the business. The main purpose of this general reserve is to absorb or offset any losses that might possibly result from future operations, or from unforeseen or unusual causes, and thereby protect the capital stock against being reduced below its par value.

Although this reserve capital is subject to being absorbed by later losses, the interest of each patron may be determined and

recorded on the books each year, or at least be determinable from the records of the association. If subsequent losses do not wipe out this reserve for any one year, and the total amount of the reserve for all years is built up until it is larger than necessary for the protection of the outstanding capital, it would then be possible for the association to pay off the interest of patrons in the oldest of these annual reserves, and continue to set up additional reserves out of current operations. By this means the interest of members in any unexhausted part of these annual reserves may be revolved in much the same way that preferred stock or other nonvoting certificates are revolved.

The cooperative statutes of some States contain provisions regarding the percentage of each year's income which must or may be set aside as a reserve by a cooperative association until the amount of such reserve equals a stated percentage of the paid-in capital. Even though not required by State statute, it is believed that the setting aside of at least 10 percent of the net earnings should be regarded as a minimum requirement. If some such reserve is not accumulated, and a loss is sustained, the face value of outstanding stock or other capital certificates will be impaired.

The payment of a limited dividend on outstanding capital tends to produce equality among the stockholders or members since some may have invested more than others in the capital of the association. ^{12/} If the amount of capital invested by each member were always exactly in proportion to his patronage, there would be no need for dividends on stock; but this is seldom if ever true, even with associations that revolve their capital. The payment of dividends on invested capital equal to a reasonable rate of interest on borrowed capital tends to cause the association to be more cooperative than it otherwise would be. The essential difference between dividends on invested capital and interest on borrowed money is that dividends on capital need not be paid unless earned, whereas interest on borrowed money is a definite annual obligation of the association regardless of income.

After the desired amount of income is set aside as a general reserve, and payment is provided for a reasonable rate of return on fully paid shares of stock, all of the net income then remaining should be allocated to the patrons as a patronage dividend. This does not necessarily mean that these patronage dividends must be paid in cash. All or part of the amounts allocated as patronage dividends may be capitalized by providing for payment to be made to the patrons in additional shares of stock, other certificates, or by book credits set up to their individual capital accounts.

^{12/} Hulbert, L. S. Legal Phases of Cooperative Associations. U. S. Department of Agriculture. Bull., 1106. October 1929.

In order to distribute patronage dividends separately by departments, it will first be necessary to deduct from the net income of each department a proportionate or arbitrary amount of the income which has been set aside as a general reserve, and also that to be used in paying dividends on invested capital. The procedure may be illustrated by the following example:

STATEMENT OF THE DISTRIBUTION OF NET INCOME

(Realized from ginning 2,000 bales of cotton, and related activities)

Item	Ginning and wrapping	Cotton-seed	Bale cotton	Total
Net income above all expenses	\$3,300.00	\$2,500.00	\$200.00	\$6,000.00
Less 10 percent to reserve	330.00	250.00	20.00	600.00
Less 4 percent on stock	220.00	167.00	13.00	400.00
For patronage returns	\$2,750.00	\$2,083.00	\$167.00	\$5,000.00

Units	Cwt. S/C	Tons	Bales
Quantities handled	34,400	850	334
Patronage return per unit	8.0¢	\$2.45	50¢

Basis of Patronage Return 13/

The income then remaining for patronage returns would be apportioned to the patrons by departments according to the amount of business contributed by each patron to each department. The income from ginning and wrapping may be apportioned in several ways. Pounds of seed cotton ginned, or total dollars paid for ginning and wrapping are usually considered more equitable than 500-pound equivalent bales or running bales. Generally the allocation should be made on the same unit basis as ginning charges. The income from cottonseed should be apportioned on a quantity basis. The income from selling cotton is usually pro rated on a per bale basis, but the number of pounds of lint, or 500-pound-equivalent bales, would perhaps be more equitable.

The total amount to be allocated to any one patron in the above illustration would be the sum of his part of the income from each of the three departments. For example, a patron who ginned 15,000 pounds of seed cotton (10 bales), and sold the association 4 tons of

13/ Paulson, W. E., and Baggett, R. T. Basis of Computing Patronage Dividend of Cooperative Cotton Gins. Journal of Farm Economics. Vol. XIX, No. 4. November 1937.

cottonseed and 3 bales of cotton would get the following patronage allocation:

Ginning 150 cwt. (15,000 pounds)	@ 8.0 cents per cwt.	\$12.00
4 tons cottonseed sold	@ \$2.45 per ton	10.80
3 bales of cotton sold	@ 50 cents per bale	<u>1.50</u>
Total patronage allocation		\$24.30

In the event that a loss was sustained in a department, it would either be necessary to deduct such loss from the income of one or more of the profitable departments before making the patronage distributions, or to apportion the loss to those who patronized the unprofitable department and deduct it from their part of the patronage distributions of profitable departments.

Distribution of Patronage Allocations

The amount of the patronage allocation of each patron which would be distributed in cash would depend on the financial condition of the association, and its policy with respect to making retains for capital purposes. It would be highly desirable to apply the first of such patronage allocation of a nonmember to payment for one share of common stock. A percentage of the amount then remaining to the credit of each of the patrons may be retained for capital purposes and distributed to them in shares of preferred stock or other certificates. The balance of the patronage allocation of each patron would then be paid to him in cash.

In addition to any per unit capital retains made at the time each bale of cotton is ginned, at least part of the net income each year should also be retained by the association for capital purposes and distributed to the patrons in preferred stock in order to provide funds for the repayment of any capital borrowed during the early years of a new association, and to revolve the preferred stock promptly thereafter. The larger the total amount retained each year, the shorter the period required to completely revolve the preferred stock. For example, an association which required \$20,000 capital could revolve its stock in 5 years after all indebtedness is paid by retaining a total of \$4,000 per year, or in 10 years by retaining \$2,000 per year.

In order to illustrate the method of distribution suggested in article X, section 2, of the bylaws (Appendix A) the following example is given. Assume that the \$5,000 available for patronage returns of the association illustrated on page 22, has been allocated to the patrons by departments and is to be distributed as follows: (1) By issuing one fully paid share of common stock to each one of four nonmember patrons, (2) by retaining 60 percent of the balance for capital purposes to be distributed to the patron in preferred

stock, and (3) by paying the remaining balance in cash. The total amount distributed in each way would be:

(1) Common stock	\$ 40.00
(2) Preferred stock	2,976.00
(3) Cash	<u>1,984.00</u>
Total	\$ 5,000.00

In addition to the \$40 common stock, there is a total of \$4,960 to be distributed in preferred stock and cash. The amount of preferred stock to be distributed to any one patron would be 60 percent of his patronage allocation after the deduction, if any, is made for the one share of common stock.

On this basis, if the individual patron whose patronage allocation was \$24.30, in the illustration on page 23, was already a paid-up member, he would receive \$14.58 in credits on preferred stock and \$9.72 in cash. On the other hand, if this patron were one of the four nonmembers, he would receive one \$10 share of common stock, \$8.58 in credits on preferred stock, and \$5.72 in cash. If the non-member were ineligible for membership, he would be treated in the same manner as a fully paid member and would receive \$14.58 in credits on preferred stock and \$9.72 in cash.

In making cash distributions it is good business on the part of the association to offset past-due accounts, notes, stock subscriptions, and other current obligations of the patron to the association. However, this practice should not be followed for that part of the patronage distribution to be made in credits on preferred stock. Such a procedure is, in effect, the same as paying that patron his dividends in cash, as the obligation of the patron is canceled, and in addition the patron does not make an investment in the capital of the association in proportion to that made by other patrons. From the standpoint of new members, however, the practice of applying all of the patronage distribution to the payment of common stock until one share shall have been acquired, is justifiable.

LEGAL BASIS

Each cotton-producing State has one or more cooperative statutes which afford farmers a legal basis for organizing cooperative associations. A cooperative gin should be incorporated under a cooperative statute peculiarly suitable for its purpose. In those States that have more than one cooperative law, the alternate provisions of each law should be compared in order to select the one most desirable for the incorporation and operation of a cooperative cotton gin. Copies of these laws may be obtained by consulting an attorney or by writing to the proper State official, usually the Secretary of State.

Although there are wide variations in the provisions of the cooperative laws of the different States, they generally will specify the following:

1. Minimum number of members required to incorporate.
2. Subjects that must be covered in the articles of incorporation.
3. The particular State official or department to which the articles of incorporation are to be sent.
4. Fees required.
5. General powers, rights, and obligations.
6. Voting rights of stockholders and members.
7. Terms and conditions of membership.
8. Nonmember relationships.
9. General provisions with respect to distribution of income.
10. Capital structure, stock or nonstock; and if stock, the classes (common and preferred); eligibility for ownership; provisions for transfer; voting rights; dividend rates; and rights on liquidation.

In addition to the requirements of State laws pertaining to cooperation, certain Federal statutes should also be considered. If a farmers' cooperative association complies with the necessary conditions, it may obtain exemption from the payment of Federal income taxes (Sec. 101, par. 12, 49 Stat. 1673; also p. 60 of this circular), surtaxes on undistributed profits (Sec. 14, par. 2, 49 Stat. 1655), capital-stock taxes (Sec. 105, 49 Stat. 1017), excess-profit taxes (Sec. 106, 49 Stat. 1019), and stamp taxes on shares of stock (45 Stat. 791). Likewise, a cooperative association that meets the definition of a cooperative association as given in Section 15 of the Agricultural Marketing Act, as amended (49 Stat. 317), is eligible to borrow from a bank for cooperatives.

ORGANIZATION PROCEDURE

Before a cooperative association is formed for the operation of a cotton gin, those who are interested in its formation should ascertain if there is a real need for a cooperative gin in the community and if conditions are favorable to its success. One of the best ways of ascertaining if a cooperative gin should be established is to hold a meeting or meetings of farmers, called by those who are sponsoring the establishment of a cooperative gin, to consider and discuss this matter. At such a meeting the chairman should encourage a frank discussion of the project by all present. Among the points to be discussed are:

- (1) The number of farmers who are or should be interested, and the prospective number of bales of cotton which probably would be delivered for ginning.
- (2) The amount of capital required, and the amount of stock subscriptions which probably could be obtained.
- (3) The size, equipment, cost and make of gin machinery that would be required.
- (4) The principles and practices that should be followed by a cooperative gin, and the benefits that might be derived.

If the information obtained at such a meeting or meetings is unfavorable to the establishment of a cooperative gin, the project should be abandoned. On the other hand, if the information is favorable, it would be in order to name a committee or possibly several committees to look after the details of organizing the association. If more than one were deemed desirable, the following committees might be appointed:

- (1) Committee on organization.
- (2) Stock subscription and survey committee.
- (3) Gin plant committee.
- (4) Special committees on other problems.

Duties of the Committees

All of these committees should work closely together in carrying out their assignments, and to that end it may be desirable to have one or more of the committeemen serve on all of the committees.

The committee on organization should have general charge of organizing the association and should be responsible for having the organization papers prepared. These would include:

- (1) Organization agreement.
- (2) Ginning agreement.
- (3) Articles of incorporation.
- (4) Waivers of notice and consent to holding meetings.
- (5) Bylaws.

The services of an attorney should be engaged for drafting these papers. Inasmuch as one object of the organization agreement is to ascertain definitely if a cooperative association should be organized for the operation of a cooperative cotton gin, it should be drafted first. If farmers controlling a sufficient amount of cotton to justify the incorporation of a cooperative association sign the organization agreement, the other papers required for its organization should then be prepared. In Appendix A of this publication will be found suggested forms for each type of organization paper. These forms are submitted only as guides and they must be altered, modified and checked to meet local factors and conditions, and the legal requirements of the State in which the cooperative association is to be incorporated.

A sufficient number of copies of the organization agreement should be made available to the members of the stock-subscription and survey committee as soon as possible in order that they may begin their work of making surveys and taking subscriptions. Attention is called to the fact that the form of organization agreement given in Appendix A (pp. 31-33) provides for subscriptions for a stated amount of common and preferred stock and for a statement of the amount of cash and notes which the subscriber gives in payment thereof, and for information showing the average cotton acreage and production of each subscriber. It may be deemed advisable to ask for other information such as the distance that each subscriber will be from the gin, and whether the subscriber is the owner of the farm which he occupies.

It is assumed, of course, that in the preparation of the various organization papers and in other matters the views of a majority of the prospective members will be reflected, insofar as they are consistent with law.

The gin plant committee will make inquiries regarding the possibilities of acquiring an existing gin plant; will correspond with manufacturers of gin machinery for the purpose of getting offers, and will also investigate the desirability of various locations for a gin. It will be remembered that the committee should not attempt to make any binding agreements, because it is not certain whether

the association will actually be incorporated and, moreover, any agreements of the committee ordinarily would not be binding on the association until they are ratified or adopted by the association.

Members of the stock subscription and survey committee should begin their work as soon as copies of the organization agreement are available. If the area to be covered is large, or the prospective members scattered, it may be advisable to assign two-men teams to specified localities, such as school districts or other geographic areas. The members of this committee should be well informed regarding information already obtained and the tentative plans for the association. It is all-important that they have a thorough understanding of the provisions and procedure under which a cooperative gin should operate. The solicitation of prospective members should be done on a frank, straightforward business basis and care should be exercised to avoid making representations or promises that are doubtful of fulfillment. If the organization committee is able to obtain signatures to the organization agreement within the stated time limit, subscribing for the minimum amount of capital stock and pledging the minimum bales of cotton for ginning, all as set forth in section 5 of the organization agreement, the organization committee should take prompt steps to have the association incorporated. In this connection, it will be remembered that articles of incorporation must conform strictly to the statute under which the association is to be incorporated. Again, every provision called for by this statute must be covered in the articles of incorporation. In most States, the persons who are to act as incorporators of an association must be producers of agricultural products and nearly all of the cooperative acts provide that the names and addresses of the first board of directors shall be included in the articles of incorporation. Usually the incorporators, or a part of them, are also named in the articles of incorporation as members of the first board of directors. Under some statutes the articles of incorporation are also required to state the persons who will constitute the first officers.

Following the filing of record of the articles of incorporation, it is in order in most of the States for those named therein as incorporators to hold a meeting (for form of waiver of notice, see Appendix A, p 55) as the stockholders or "charter members" of the association for the purpose of adopting bylaws.

Nearly all of the statutes under which cooperative associations are incorporated provide that a majority vote of the members or stockholders or their written assent is necessary for the adoption of bylaws. The persons named in the articles of incorporation as incorporators are generally regarded as members or stockholders of the association on the filing of the articles of incorporation; while further action is usually required for making members or stockholders of other persons who have subscribed for stock, or who have agreed to become members. For convenience in the organization of cooperative associations the "charter" members or stockholders usually adopt the original bylaws. In the form of bylaws, (Appendix A, pp. 41-52)

provision is made for having each incorporator sign the bylaws for the purpose of assenting thereto. This should be done at the meeting for the adoption of the bylaws. A form of minutes for this meeting will be found on p. 55. Under some statutes, bylaws are adopted by the incorporators as incorporators, and if an association is incorporated under such a statute the forms shown on pages 55 and 57 should be changed accordingly. Likewise, if the first board of directors is not named in the articles of incorporation and the incorporators are authorized to elect them, the forms should reflect this fact.

After the bylaws of the association have been adopted, the board of directors named in the articles of incorporation should hold a meeting. This meeting is usually held in pursuance of a waiver of notice of meeting (Appendix A, p. 56).

Among the things which should be acted upon by the board of directors at this meeting (suggested minutes of which appear on page 58) are the following:

- (1) Election of officers specified in the bylaws.
- (2) Instructions to the president and secretary to obtain stock certificates and to issue the same.
- (3) Authorization of the president and secretary to have copies of the articles of incorporation and bylaws printed and distributed to members.
- (4) Adoption of the form of ginning agreement.
- (5) Acceptance of all of the subscription agreements for capital stock of the association; authorization of the president and secretary to enter into ginning agreements with subscribers to common stock; and authorization of officers to obtain additional subscriptions for capital stock and additional signatures to ginning agreements.
- (6) Selection of a depository bank.
- (7) Designation of officers or employees who are to be authorized to sign checks.
- (8) Arrangements for the bonding of officers and employees in accordance with the bylaws.
- (9) Instructions to the secretary to obtain a corporate seal in form as provided in the bylaws.
- (10) Transaction of any other business relating to such matters as insurance and the employment of a manager and other employees.

APPENDIX A

Suggested Organization Forms

In Appendix A of this publication will be found forms designed for use in forming a cooperative gin association with common and preferred stock. The ownership of common stock is restricted to one share for each producer. Consequently, the principle of one vote for each member is preserved, even in those States where each share of common capital stock carries a vote. The preferred stock carries no vote, and any number of shares may be held by any one.

On pages 31-33 is a suggested form of organization agreement. An organization agreement is not indispensable to the formation of a cooperative gin association and in practice such associations are generally organized without the use of it. If such an agreement is not used other means must be employed to ascertain if the facts justify the formation of an association. Again, when deemed advisable, a form of organization agreement less comprehensive than the one on pages 31-33 may be used.

The form of ginning agreement which the organization agreement requires to be attached thereto should convey to prospective members of the association who sign the organization agreement an understanding of substantially the form of agreement that they will be required to execute when the organization of the association is completed. It follows that the ginning agreement which the board of directors finally adopts should not differ materially from the form attached to the organization agreement. On pages 34-35 is a form of ginning agreement which should be helpful in preparing such an agreement.

The forms are intended primarily to illustrate the character of provisions deemed appropriate for cooperative associations operating gins, due consideration being given to the fact that such associations are local institutions which operate with relatively small memberships and over a comparatively small area for only a few months in each year; and these forms in any given State must be adapted to the statutory requirements thereof by a competent attorney.

In forming a cooperative gin, it is necessary to see that State laws applicable to the sale of stock, popularly known as "blue sky" laws are complied with, and to see that the association has the minimum paid-in capital required by law, and that stock subscribers pay at least the minimum required by law on their stock subscriptions.

Particular attention is directed to the provisions of Articles X and XI of the suggested bylaws, which provide for the revolving capital plan of financing, and which involve the issuance of preferred stock to evidence retentions for capital purposes, and the retirement thereof as funds are available for that purpose. In lieu of issuing preferred stock to evidence retentions, a certificate of interest or a certificate of indebtedness may be used. Certificates of interest or indebtedness have certain advantages in that they may

be issued to evidence any specific sum of money, and in this respect, differ from preferred stock certificates, which have a prescribed par value. Likewise, it may be found simpler to retire certificates of interest on a pro rata basis by making partial payments which are endorsed on the back of the certificate than it is to retire preferred stock certificates on a pro rata basis by partial payments. Also, in States where preferred stock carries a right to vote, it is necessary to use certificates of interest in order to prohibit "non-members" from voting.

While it is believed that the use of certificates of interest may, in particular instances, be regarded as a preferable method of effectuating a revolving-capital plan of financing, these forms have been prepared with a view to revolving preferred stock, in recognition of the fact that most cooperative associations operating gins, at the present time, prefer to issue stock. It is not necessary to issue either stock certificates or certificates of interest to evidence retentions for capital purposes as an association may rely on proper book entries, but generally speaking, the declaration of a patronage dividend which is evidenced by some form of a certificate is preferable.

ORGANIZATION AGREEMENT

for Cooperative Gin at _____

_____.

We, the undersigned, all of whom are residents of the State of _____, engaged in the production of cotton, together with signers of agreements identical herewith, to promote, foster, and encourage the ginning of cotton cooperatively, propose to organize a cooperative gin association at _____, with capital stock under the _____ laws of the State of _____, and to acquire suitable facilities therefor by purchasing _____

(Here describe property to be acquired)

at a cost of not exceeding \$_____.

The undersigned, each for himself and collectively for the express benefit of and for the association to be organized and in consideration of the premises and of the subscriptions of others to agreements identical herewith, hereby covenant and agree with each other as follows:

(1) The association shall be organized with suitable articles of incorporation and bylaws, under the guidance of an organization committee, consisting of the following persons:

<u>Name</u>	<u>Address</u>

If any member or members of this committee shall resign or be unable to act, the remainder of the committee may elect a successor to fill any such vacancy or the committee may increase its membership if deemed necessary.

(2) The organization committee shall keep a full, true and detailed account of all receipts and of all expenditures of every kind and shall have such accounts audited and render a written report thereof to the board of directors of the association, when organized, and shall thereupon turn over to the association any balance remaining in its hands free of obligation. If it is not so organized, such unexpended balance shall be prorated among those who contributed thereto.

(3) The amount of the capital stock shall be \$_____, divided into _____ shares of common stock, each of the par value of \$_____, and _____ shares of preferred stock, each of the par value of \$_____.

(4) The undersigned agree to purchase and do hereby subscribe for the amount and kind of capital stock set opposite our respective names, and agree to pay for same as follows:

(Here insert the plan of stock payment to be used)

(5) If, on or before _____, 19____, bona fide subscriptions from acceptable parties to the common and preferred stock of the association shall equal the sum of \$_____ and producers of cotton whose average annual production aggregates at least _____ bales of cotton, have agreed to execute ginning agreements covering their cotton crops, the organization committee shall forthwith proceed to file the articles of incorporation and to have the organization of the association completed; subject, however, to the foregoing conditions only; the undersigned agree that their signatures hereto are irrevocable and they so agree in order to induce others to sign this or similar agreements for their mutual benefit.

(6) Acceptance of this agreement by the association shall be deemed conclusive upon the mailing of notice to that effect to the undersigned, at our respective addresses listed hereon, and such notice shall be conclusively established by the affidavit of the secretary of the association. Upon receipt of such notice, the undersigned shall promptly tender to the association the respective amounts subscribed for common and preferred stock or the initial payments required thereon.

(7) The undersigned represent that the average annual acres of cotton harvested and the average annual bales produced for the past _____ years are set forth opposite our respective names.

(8) The undersigned agree that we will become members of the association when formed by executing ginning agreements, the terms of which shall be similar to the terms contained in the form attached hereto and made a part hereof.

IN WITNESS WHEREOF, we have hereunto set our hands as of this

_____ day of _____, 19____.

Stock Subscription				Cotton Crop (____ Year Average)	
Signature	Address	Shares Common	Shares Preferred	Acres Grown	Bales Made

GINNING AGREEMENT

This Agreement, between the _____ Association, hereinafter called the "Association," and the undersigned, hereinafter called the "Grower,"

W I T N E S S E T H:

(1) The Grower agrees to deliver to the Association for ginning all cotton produced by or for him, and to sell to the Association or otherwise deliver to it for marketing or for processing, either through its own facilities or by a cooperative oil mill all the seed from said cotton, except cottonseed retained for planting or home use, or which, on request of the Grower, shall be excepted herefrom by order of the board of directors of the Association.

(2) The Grower hereby expressly authorizes and directs the board of directors of the Association to fix the charges for ginning, wrapping, drying or otherwise processing or handling cotton and cottonseed, the price to be paid for cottonseed, and the amount to be paid per bale to the Association by Grower for capital purposes to be evidenced by preferred stock, which shall not exceed \$_____ per bale of cotton ginned; and the Association shall make such advances on cottonseed, other than that purchased by the Association, as may be found practicable.

(3) The Association may borrow money for its own account and pledge all of such cottonseed as security therefor without limitation and the Association is authorized to sell such cottonseed when and as it deems best.

(4) The Association may enter into agreements with other growers differing in terms from those contained herein, but consistent with the bylaws of the Association, without invalidating this Agreement provided that the Grower, at his request, may execute a similar agreement as a substitute for this contract.

(5) Inasmuch as the remedy at law would be inadequate and inasmuch as it would be impracticable and extremely difficult to determine the actual damage resulting to the Association should the Grower fail to deliver his cotton hereunder, regardless of the cause of such failure, the Grower hereby agrees to pay to the Association for all cotton delivered elsewhere for ginning by or for him, other than in accordance with the terms hereof, the sum of _____ cents per _____ on all cotton so delivered, as liquidated damages for the breach of this contract; all parties agreeing that this contract is one of a series dependent for its true value upon the adherence of each and all of the contracting parties to each and all of the said contracts, but the cancelation of this contract or the failure of the Grower to comply therewith shall not affect other similar contracts. 14/

14/ There is a difference of opinion as to the desirability of including these provisions.

(6) If the Association brings any action whatsoever by reason of a breach or threatened breach hereof, the Grower shall pay all costs of court, costs for bonds and otherwise, expenses of travel and all expenses arising out of or caused by the litigation, and reasonable attorney fees expended or incurred by it in such proceedings and all such costs and expenses shall be included in the judgment. 14/

(7) It is agreed that the articles of incorporation and the bylaws now or hereafter in effect, and this contract constitute the entire agreement between the Association and the Grower.

(8) After this agreement shall have been in effect _____ years from the date of its acceptance by the Association, either party hereto may terminate it in any year on the last day of the anniversary month in which this agreement was so accepted by notifying the other party in writing of this intention, such notice to be given between the first and fifteenth of the month immediately prior to the effective date of termination. If neither of the parties hereto terminates this agreement in any year, as aforesaid, it is hereby mutually agreed that this shall constitute conclusive evidence that the parties hereto have renewed this agreement for another year.

(9) The parties agree that there are no oral or other conditions, promises, covenants, representations or inducements in addition to or at variance with any of the terms hereof; and that this Agreement represents the voluntary and clear understanding of both parties fully and completely.

Read, considered and signed at _____, _____
this _____ day of _____, 19____.

Grower's signature _____ (_____)
(Do not sign without reading) (Print Grower's name here)

Address _____ (_____)
(R.F.D. or Street No.) (Town)

County _____ State _____

Accepted at _____, _____ this _____
day of _____, 19____, in accordance with a resolution
of the board of directors.

_____ Association

By _____
Secretary

14/ There is a difference of opinion as to the desirability of including these provisions.

ARTICLES OF INCORPORATION

of

Association 15/

WE, THE UNDERSIGNED, all of whom are residents and citizens of the State of _____, engaged in the production of agricultural products, do hereby voluntarily associate ourselves together for the purpose of organizing, incorporating and operating a cooperative association with capital stock under the provisions of _____

of the State of _____, and amendments thereto, with all the rights, powers, privileges, benefits and immunities given or permitted corporations so formed; and for that purpose hereby adopt these Articles of Incorporation:

ARTICLE I

The name 16/ of the association shall be _____

ARTICLE II

The association is formed for the purpose of engaging in the following activities:

(a) Ginning, wrapping and otherwise processing cotton, and/or processing cottonseed and other farm products.

(b) Buying, selling, storing, shipping, hauling and otherwise handling cotton, cotton seed and cottonseed products and/or other farm products and the byproducts thereof.

(c) Buying, selling, dealing in and handling (1) bagging, ties and all other supplies necessary and incidental to ginning cotton, (2) any articles, materials and supplies used in processing and/or handling other farm products, or the byproducts thereof, and (3) any farm materials, supplies and equipment.

15/ Articles of incorporation must strictly meet the requirements of the law of the State in which an association is being incorporated and this form must be changed accordingly.

16/ Some States have restrictions regarding names, and particularly on the use of the word "cooperative."

ARTICLE III

The association shall have the following powers:

- (a) To transact business with nonmembers, provided the business transacted with such nonmembers is not greater in value than that transacted with its members. 17/
- (b) To act as the agent or representative of any patron or patrons in any of the activities mentioned in Article II hereof.
- (c) To buy, acquire, hold, own, lease, give as security, sell and otherwise dispose of, and exercise all privileges of ownership over real and personal property of any character, and/or interest therein, as may be deemed necessary or desirable for the conduct of the business of the association, or incidental thereto.
- (d) To borrow money for any purpose of the association without limitation, and to issue notes, bonds, debentures or other obligations therefor which may be secured in any manner permitted by law. 18/
- (e) To buy, hold, retire, and dispose of its own capital stock in accordance with the law.
- (f) To establish reserves and invest the funds thereof, or any other funds of the association, in bonds or in such other property as may be specified in the bylaws.
- (g) To guarantee, endorse, purchase or otherwise acquire, hold, sell, assign, transfer, mortgage, pledge or otherwise dispose of shares of stock, bonds, or other evidences of indebtedness of any corporation or association engaged in any related activity, and to vote, cooperate and share in the management or control of such organization, its activities and affairs.
- (h) To participate by membership, stock ownership, contract or otherwise, in the management of cooperative agencies for the furthering of any of the purposes of this association.
- (i) To do each and every thing necessary, suitable or proper for the accomplishment of any of the purposes or the attainment of any one or more of the objects herein enumerated; or conducive to or expedient for the interest or benefit of the association; and to contract accordingly; and in addition, to exercise and possess all powers, rights, and privileges, necessary or incidental to the

17/ In some States this provision must be omitted or modified to meet the requirements of the statute.

18/ Under some statutes the maximum amount of corporate indebtedness that may be incurred must be stated in the articles of incorporation.

purposes for which the association is organized, or to the activities in which it is engaged, and to have and exercise all the powers, privileges and rights granted, authorized or allowed to associations organized under _____ and amendments thereto, and all other powers authorized or allowed to corporations by other laws of the State of _____, insofar as they are not in conflict with the express provisions of the law under which the association is organized.

ARTICLE IV

The association shall have its principal place of business in the City of _____, County of _____, State of _____.

ARTICLE V

The term for which this association shall exist is _____ years from and after the date of its incorporation.

ARTICLE VI

The management of the business and affairs of the association shall be vested in a board of directors consisting of ^{19/}_____ members, each of whom shall be a holder in good standing of one fully paid share of common stock of the association. Directors shall be elected at each annual meeting of the stockholders of the association, for terms ending at the next annual meeting, and unless sooner removed by death, resignation, or for cause, they shall hold office until their successors have been elected and qualified. The names ^{20/}_____ and addresses of those who are to serve as incorporating directors until the first annual meeting of the stockholders, or until their successors are elected and qualified are:

<u>Name</u>	<u>Address</u>
_____	_____
_____	_____
_____	_____
_____	_____
_____	_____

^{19/} If the statute under which an association is to be incorporated will permit, it is preferable to state in the articles of incorporation only the minimum number of directors that the association will have, providing in the bylaws, which may be more easily amended, for the actual number.

^{20/} Some statutes do not require that the names of the original directors be given in the articles of incorporation.

ARTICLE VII

Section 1. The amount of the authorized capital stock shall be _____ Dollars (\$ _____), divided into _____ shares of common stock, each of the par value of _____ Dollars and _____ shares of preferred stock, each of the par value of _____ Dollars.

Section 2. The common stock of the association shall only be issued or transferred to, or held by producers of agricultural products who agree to patronize the association, in accordance with uniform terms and conditions prescribed thereby in a ginning agreement, and no person, firm, or corporation shall own or hold at any one time more than one share of such common stock, or shall have more than one vote in transacting business at meetings of the stockholders. The common stock shall not bear dividends. The common stock shall only be transferred upon approval of the board of directors. No purported transfer of common stock shall pass any right or privilege on account of such stock, or any vote or voice in the control or management of the association unless the recipient thereof is eligible, as herein defined, to hold such stock, and such transfer is approved by the board of directors. The voting rights of any holder of common stock who ceases to be eligible to hold such stock, or who violates any of the terms and conditions of the uniform ginning agreement, bylaws, or rules and regulations of the association, or who performs an act of disloyalty to the association, may be suspended by action of the board of directors following a hearing held as provided in the bylaws. In any case in which the voting rights of any holder of common stock have been suspended by the board of directors, the association shall have the right, at its option (a) to purchase such stock at its book or par value, whichever is less, as determined by the board of directors of the association, (b) to require the transfer of any such stock at such book or par value to any person or association eligible to hold the same or (c) to require such holder of any such stock to convert the same into shares of preferred stock of equal par value.

In exercising its right to purchase or require the transfer or conversion into preferred stock of common stock, if such holder fails to deliver the certificate or certificates evidencing the same, the association may cancel such certificate or certificates on its books and issue a new certificate or certificates of common or preferred stock, as the case may be, to the party entitled thereto.

Section 3. The preferred stock of the association shall bear noncumulative dividends not exceeding _____ percent per annum, if earned and when declared by the board of directors; and such dividends shall have preference over any and all other dividends or distributions declared in any year. At the discretion of the board of directors, all dividends on preferred stock, or any part thereof, may be paid in additional certificates of preferred stock and/or credits on preferred stock. The preferred stock shall carry no

voting rights 21/ and such stock, or any part thereof, may be redeemed or retired upon call of the board of directors from time to time provided said stock is called and retired in the same order as originally issued. All such preferred stock so retired shall be paid for in cash at the par value thereof, plus any dividend declared thereon and unpaid; and such stock shall not bear dividends after the date fixed in the call for its retirement. Upon distribution of the assets of the association in the event of dissolution or liquidation, the holders of preferred stock shall be entitled to receive the par value of their preferred stock, plus any dividend declared thereon and unpaid, before any distribution is made on common stock.

Section 4. All transfers of stock shall be made on the books of the association only on surrender of the certificate covering the same by the holder thereof, or by attorney properly authorized. The association shall have a lien on all stock, and on any dividends declared thereon, for all indebtedness of the holder thereof to the association. In the event of dissolution or liquidation of the association, no holder of stock shall be entitled to receive any distribution of the assets on such stock in excess of the par value thereof, plus any dividend declared thereon and unpaid; and any assets remaining after the payment of all debts, and the retirement of all stock and credits on stock, at par value, shall be distributed on a patronage basis as provided in the bylaws.

IN TESTIMONY WHEREOF, we have hereunto set our hands this _____ day of _____, 19____.

_____	_____
_____	_____
_____	_____
_____	_____
_____	_____

[There should be added the statutory form of acknowledgment to be executed by those incorporators who, under State law, are required to acknowledge the execution of the articles of incorporation.]

BYLAWS

of the

ARTICLE I

Powers and Purposes

The powers and purposes of this association are those set forth in the articles of incorporation. The articles of incorporation shall control in the event of any conflict between its provisions and any part of these bylaws.

ARTICLE II

Capital Stock

The authorized capital stock of the association as set forth in the articles of incorporation shall have such voting rights, bear such dividends, and be issued, transferred, redeemed or retired as provided in article VII of said articles of incorporation. Sections 2 and 4 of article VII of the articles of incorporation shall be printed verbatim on each certificate of common stock and sections 3 and 4 of article VII of the articles of incorporation shall be printed verbatim on each certificate of preferred stock.

ARTICLE III

Membership

Section 1. Qualifications. -- Any person, firm or corporation, including landlords who receive as rent a part of the crop raised on leased premises, engaged in the production of agricultural products may, subject to the approval of the board of directors, become a member of this association by acquiring one share of the common stock thereof, and by entering into a ginning agreement with the association in the form prescribed by the board of directors.

Section 2. Suspension of voting rights. -- The voting rights of any holder of common stock who ceases to be eligible to hold such stock shall be suspended immediately upon the finding of the board of directors that such holder is ineligible to hold such stock; and the voting rights of any holder of common stock who violates any of the terms and conditions of the uniform ginning agreement, bylaws, or rules and regulations of the association, or who fails to observe

any obligation or duty of a holder of such stock, may be suspended by a majority vote of the board of directors; provided, however, that before the voting rights are suspended for any cause, the board of directors shall hold a meeting for the purpose of hearing and receiving evidence of the charges preferred against him; and at such meeting, he shall have the right to present witnesses and be heard in person or by counsel in answer thereto; and the person bringing the charges against him shall have the same opportunity. Notice of such meeting, containing a statement of the charges preferred against a holder of common stock, shall be mailed to such holder at least ten days previous to the date of the meeting. A holder of common stock whose voting rights have been suspended by the board of directors shall thereafter be deemed a member not in good standing, and as such, ineligible to serve the association as a director or officer thereof.

In any case in which the voting rights of any holder of common stock have been suspended by the board of directors, the association shall have the right, at its option (a) to purchase such stock at its book or par value, whichever is less, as determined by the board of directors of the association, (b) to require the transfer of any such stock at such book or par value to any person or association eligible to hold the same or (c) to require such holder of any such stock to convert the same into shares of preferred stock of equal par value.

In exercising its right to purchase or require the transfer or conversion of common stock into preferred stock, if such holder fails to deliver the certificate or certificates evidencing the same, the association may cancel such certificate or certificates on its books and issue a new certificate or certificates of common or preferred stock, as the case may be, to the party entitled thereto.

ARTICLE IV

Nonmember-Patrons

The association may transact business with nonmembers, provided the business transacted with such nonmembers is not greater in value than that transacted with its members. 22/

ARTICLE V

Stockholders' Meetings

Section 1. Annual meeting. -- The annual meeting of the stockholders of this association shall be held in its office in the town of _____, at _____ o'clock _____ M., on the _____

22/ In some States, this provision must be omitted or modified to meet the requirements of the statute.

in _____ of each year, if not a legal holiday, and if a legal holiday, on the next business day following; provided that the place and/or time for holding any annual meeting may be changed by the board of directors to any place within said town, and to any other time during said day.

Section 2. Special meetings. -- Special meetings of the stockholders of this association may be held at any time when called in manner as hereinafter provided. The board of directors shall designate the date, time and place for holding all special meetings, but such place shall be in the town of _____. Special meetings may be called at any time by the board of directors, and shall be called by said board whenever a written request containing a statement of the specific business to be considered, signed by at least _____ percent of the holders of fully paid-up common stock, provided that in no case shall the required number of signatures to such request be less than _____; and upon receipt of such request the board of directors shall order a meeting held within thirty days from the date of such receipt. The purpose of every special meeting shall be stated in the notice thereof, and no business shall be transacted thereat except such as is specified in the notice.

Section 3. Notice of meetings. Written or printed notice of all meetings of the stockholders, stating the nature, time, place and purpose thereof, shall be mailed to each holder of fully paid-up common stock to the address shown on the books of the association, or handed to such stockholder, at least _____ days prior to the time for holding the meeting.

Section 4. Voting rights and quorum. -- Only holders of fully paid-up common stock in good standing shall have the right to vote at meetings of the stockholders, and no holder of such stock shall have more than one vote. _____^{23/} percent of the holders of fully paid-up common stock, present in person, shall constitute a quorum for the transaction of business at any meeting of the stockholders of this association; and a vote of the majority of such stockholders present at such meeting shall be sufficient to pass or reject any measure properly placed before the meeting, except for the transaction of business for which a different quorum and a different vote is specifically provided for by statute or by these bylaws.

Section 5. Voting by proxy.^{24/} -- Voting by proxy is prohibited.

^{23/} If permitted by law the number of stockholders necessary to constitute a quorum should be small, in order that meetings may not fail for lack of a quorum.

^{24/} The right of a stockholder to vote by proxy is granted in some States.

Section 6. Order of business. -- The order of business at the annual meeting and at other meetings of the stockholders, as far as practicable, shall be:

1. Calling to order.
2. Proof of due notice of meeting.
3. Proof of quorum.
4. Reading and action on any unapproved minutes.
5. Reports of officers and committees.
6. Election of directors.
7. Unfinished business.
8. New business.
9. Adjournment.

ARTICLE VI

Board of Directors

Section 1. Number and qualifications. -- The business and affairs of this association shall be conducted and managed by a board of directors consisting of _____ members, each of whom shall be a member in good standing of the association and the owner of one fully paid-up share of common stock. No person engaged in business in competition with the association shall be eligible to serve as a director.

Section 2. Election and term of office. -- Directors shall be elected at each annual meeting of the stockholders for terms ending at the next annual meeting. And, unless they shall resign, die, become disqualified or be removed in the manner provided in section 6 hereof, they shall hold office until their successors have been elected and qualified.

Section 3. Meetings. -- As soon as practicable and within ten days following the annual meeting of the stockholders each year, the board of directors elected thereat shall hold a regular meeting at such time and place in the town of _____, as may be designated by the president. Special meetings of the board may be held at any time when called in the manner hereinafter provided. Such special meetings shall be called upon order of the president, or upon written request of a majority of the directors. The president or directors in ordering the call shall designate the date, time and place for holding the meeting, but such place shall be in the town of _____. Any business of the association may be transacted at any special meeting of the board whether or not such business is stated in the call.

Section 4. Notice of meetings. -- Written notice of regular and special meetings, stating the time, place, and purpose thereof, shall be mailed or handed to each director at least _____ days prior to the time for holding the meeting; provided, however, that directors may waive, in writing, notice of any meeting.

Section 5. Vacancies. -- Vacancies in the board of directors, other than by expiration of term, shall be filled by a majority vote of the remaining directors in office. Directors to fill such vacancies shall be elected for the unexpired term of those whom they succeed.

Section 6. Removal of directors. -- Whenever any director of the association shall cease to be eligible for the office of director, as defined in section 1 of this article, his membership on the board of directors shall terminate. Any director of the association may be removed from office by a vote of a majority of the holders of fully paid-up common stock in good standing, present in person, at any special meeting called for that purpose, at which a majority of such stockholders shall be present. Special meetings of the stockholders for voting upon the removal of a director shall be called only when a holder of common stock brings charges against such director by filing them, in writing, with the secretary of the association, together with a petition signed by _____ percent of the holders of common stock, in good standing, requesting the removal of the director in question. The director against whom such charges have been brought shall be informed in writing of the charges at least _____ days previous to the meeting and shall have an opportunity at the meeting to present witnesses and be heard in person or by counsel in answer thereto; and the person or persons bringing the charges against him shall have the same opportunity. Any vacancy created by such termination or removal from office shall be filled in the manner provided in section 5 hereof.

Section 7. Quorum. -- A majority of the members of the board of directors shall constitute a quorum for the transaction of business at any meeting of the board; and a vote of the majority of the members present at such meeting shall be sufficient to pass or reject any measure properly placed before the meeting, except for the transaction of business for which a different vote is specifically provided, by statute or by these bylaws.

Section 8. Compensation, employment and contracts. -- The members of the board of directors shall receive no compensation for their services as members of the board, but may receive a reasonable per diem to cover necessary expenses while engaged in the business of the association. No member of the board of directors and no member of his immediate family shall be employed by the association for more than thirty days in any year, unless such employment is unanimously approved by the board of directors. No member of the board of directors during his term of office, shall have any contract, arrangement, or agreement for profit with the association differing in terms or purpose from contracts, arrangements, and agreements accorded other members.

Section 9. Referendum. 25/ -- Upon demand of one-third of the entire board of directors, any matter that has been approved or

25/ There is a difference of opinion regarding the advisability of including this section unless required by statute.

passed by the board must be referred for decision to a special meeting of the stockholders, which shall be called for that purpose, or to the annual meeting if same is to be held within thirty (30) days from such demand. The decision on such matter at said meeting shall be binding upon the board of directors.

ARTICLE VII

Duties and Powers of Directors

Section 1. Management of business. -- The board of directors shall have general supervision and control of the business and affairs of the association and shall make all rules and regulations, not inconsistent with law or with these bylaws, for the management of the business and guidance of the officers, employees and agents of the association. They shall have installed an accounting system which shall be adequate to the requirements of the business, and it shall be their duty to require proper records to be kept of all business transactions.

Section 2. Employment of manager. -- The board of directors shall have the power to employ and dismiss or to authorize the employment and dismissal of a manager and such other employees as may be deemed necessary, and to fix their compensation. The manager shall have charge of the business of the association under the direction of the board of directors. No director shall serve as manager, unless unanimously approved by the board of directors.

Section 3. Bonds and insurance. -- The board of directors shall require the manager and all other officers, agents, and employees charged by the association with responsibility for the custody of any of its funds or negotiable instruments to give adequate bonds. Such bonds, unless cash security is given, shall be furnished by a responsible bonding company and approved by the board of directors, and the cost thereof shall be paid by the association. The board of directors shall provide adequate insurance covering loss of, or damage to the property of the association and property in its possession and custody for which it is liable, by fire, tornado, or wind-storm, and in addition insurance covering liability for accidents to all employees and the public.

Section 4. Ginning agreements. -- The board of directors shall prescribe and adopt the form of ginning agreement to be entered into by the association with its members which shall be for a period not to exceed _____ years, but may provide for the renewal thereof if notice of termination is not given within a specified time each year. The board of directors shall have the power to carry out such ginning agreements in every way advantageous to the association, representing the producers collectively. A separate service agreement may be adopted, in the discretion of the board of directors, for each activity in which the association may engage.

Section 5. Depositary. -- The board of directors shall have the power to select one or more banks to act as depositories of the funds of the association and to determine the manner of receiving, depositing and disbursing the funds of the association and the form of checks and the person or persons by whom same shall be signed, with the power to change such banks and the person or persons signing such checks and the form thereof at will.

Section 6. Borrowing money. -- The officers of the association who are authorized to do so by the board of directors of the association may borrow money for and on behalf of the association for any association purpose on open account or otherwise, with or without security, in such amounts and upon such terms and conditions as may from time to time appear advisable, subject to any legal requirements applicable thereto. 26/

Section 7. Investments. -- The board of directors shall have the right and power to invest any funds of the association not needed in the operation of the business, including reserve funds, in bonds or in such other property as it may deem advisable.

Section 8. General powers of board of directors. -- The board of directors of the association shall have the power and authority consistent with law, the articles of incorporation and these bylaws to provide for the carrying out of the contracts and agreements of the association and to authorize officers thereof to enter into contracts and agreements on behalf of the association and to authorize any and all acts that are deemed conducive to furthering the purposes for which the association is formed, except that the board of directors shall not have authority to sell and convey the real property, machinery, or equipment of the association without being authorized by a meeting of the holders in good standing of fully paid-up common stock, unless such conveyance is for the purpose of securing an indebtedness or the sale is of machinery, or equipment not used in the operation of the business, or unless the sale is made for replacement purposes. 26/

ARTICLE VIII

Officers

Section 1. Officers and qualifications. -- The officers of the association shall be a president and a vice president, each of whom shall be a member of the board of directors; a secretary-treasurer, or a secretary and a treasurer, who may or may not be directors or stockholders of the association; and such other officers as the board of directors deems necessary. 27/

26/ In some States there are statutory restrictions which must be met on the mortgaging of property.

27/ See statutory provisions on election and qualifications of officers.

Section 2. Election and term of office. -- All officers shall be elected by the board of directors for terms not extending beyond the first regular meeting of the board of directors following the next annual meeting of the stockholders and, unless sooner removed by death, resignation, or for cause, they shall hold office until their successors have been elected and qualified.

Section 3. Removal of officers. -- Any officer of the association required to be a member thereof, whose right to vote as a member of the association has been suspended or who has ceased to be qualified to act as a director of the association, shall thereupon cease to be an officer. The board of directors may remove any officer by a majority vote at any meeting of the board; and the stockholders may remove any officer in the same manner as directors may be removed as provided in section 6 of article VI hereof.

Duties of Officers

Section 1. Duties of president. -- The president shall preside over all meetings of the stockholders and the board of directors; call special meetings of the board of directors; perform all acts and duties usually performed by an executive and presiding officer; serve as an ex-officio member of all committees of the association; sign all stock certificates and such other documents and papers as he may be authorized to sign by the board of directors; provided, the board of directors may authorize any person to sign any or all checks, contracts and other instruments in writing on behalf of the association. The president shall perform such other duties as may be prescribed by the board of directors.

Section 2. Duties of vice president. -- In the absence or disability of the president, the vice president shall perform the duties of the president; provided, however, that in case of death, resignation, disqualification or disability of the president, the board of directors may declare the office vacant and elect his successor.

Section 3. Duties of secretary-treasurer. -- The secretary-treasurer shall keep a complete record of all meetings of the stockholders and of the board of directors. He shall have general charge and supervision of the books and records of the association, and shall perform such duties with respect to the finances of the association as may be prescribed by the board of directors. He shall sign all stock certificates and such other papers pertaining to the association as he may be authorized or directed to do by the board of directors. He shall serve all notices required by law and these bylaws and shall make a full report of all matters and business pertaining to his office to the stockholders at the annual meeting. He shall provide for the keeping of proper stock and patron records,

showing the name of each stockholder and patron of the association, the number of his stock certificate and ginning agreement, and date of issuance, surrender, cancellation, or forfeiture thereof. He shall keep the corporate seal and affix said seal to all papers requiring a seal. He shall make all reports required by law, and shall perform such other duties as may be required of him by the association or the board of directors. Upon the election of his successor, the secretary-treasurer shall turn over to him all books and other property belonging to the association that he may have in his possession. If the offices of secretary and treasurer are held by different persons, the board of directors shall prescribe the duties and responsibilities of each.

Section 4. Duties of other officers. -- Any other officers elected to offices created by the board of directors shall perform such duties with respect to such offices as may be prescribed by the board of directors.

ARTICLE X

Determination and Distribution of Income

Section 1. Audits. -- The board of directors shall have a complete audit made of the books and accounts of the association for the fiscal year ending _____ of each year, and for that purpose shall employ a competent and disinterested public auditor or accountant, who shall render a report in writing thereon, which report shall be submitted to the members at their annual meeting. In addition to a balance sheet and a statement of the total net income, such report shall show separately the net earnings or losses from ginning and wrapping cotton, from handling cottonseed, and from all other activities of the association by departments as classified by the board of directors, after all salaries, taxes, licenses, insurance and bond premiums, interest, depreciation, repairs necessary and incidental to restore the physical properties to reasonable operating condition, and all other expenses have been paid or provided for to the close of the fiscal year.

Section 2. Allocation and distribution of net income. -- The total net income so determined shall be allocated and distributed in the following order and manner:

(a) An amount, not less than _____ percent of the total net income shall be set aside each year as a general reserve until the amount of such reserve shall equal at least _____ percent of the par value of outstanding capital stock. ^{28/}

(b) An amount not exceeding _____ percent of the par value of preferred stock outstanding shall be set aside for payment of dividends on such stock.

^{28/} Statutory requirements concerning reserves should be complied with.

(c) The amounts set aside for the general reserve and for payment of dividends on preferred stock shall be deducted pro rata from the income of each department of the association and the balance of the net income then shown for each department shall be allocated to the patrons of each of the departments on the basis of their patronage.

(d) From the net amount allocated to each nonmember patron, eligible for membership in the association and approved by the board of directors, there shall first be deducted the par value of one share of common stock, or the unpaid balance due thereon; and when any such patron has complied with all the conditions for membership, a certificate for common stock paid for in this manner shall be issued to him.

(e) 29/ At least _____ percent of the amount, as determined by the board of directors, then remaining to the credit of each patron shall be retained by the association for capital purposes and distributed to him in credits on paid-in preferred stock, and the association shall issue certificates for all such shares of preferred stock fully paid for in this manner.

(f) Any remaining balance of the patronage allocations of each patron may then be paid to him in cash.

Section 3. Interest of patrons in general reserve. -- The books of the association shall be kept in such manner that the interest of each patron in the amount carried to the general reserve each year may be ascertained at any time. In the event of a net loss in the operation of the association for any one year, such loss shall be charged against these annual reserves, in an equitable manner as determined by the board of directors. Whenever the total amount of the general reserve exceeds _____ percent of the outstanding stock, the board of directors may apply such excess to paying off ratably by years the oldest unexhausted interests of the patrons therein.

Section 4. Application of cash distributions to indebtedness. -- Any part or all of the cash dividends on capital stock, cash patronage distributions, and/or cash payments for retirement of stock payable to any stockholder or patron may be applied, at the discretion of the board of directors, to the payment of any indebtedness of such stockholder or patron to the association that may be due.

29/ If it is desired to retain a fixed amount per bale instead of a percentage of net income for capital purposes, the following should be substituted for subsection (e):

At least _____ for each bale ginned for each patron shall be deducted from the amount then remaining to his credit and shall be retained by the association for capital purposes, but if such amount is insufficient to permit of such deductions all such amount shall be so retained, and distributed to the respective patrons in credits on preferred stock, and the association shall issue certificates for all such shares of preferred stock fully paid for in this manner.

ARTICLE XI

Issuance and Redemption of Preferred Stock

At the end of each fiscal year the board of directors shall issue to each patron preferred stock to evidence the amounts paid in by such patrons, on a per bale basis, for capital purposes, as provided in section 2 of the Ginning Agreement, in addition to preferred stock which it issues on account of patronage earnings, as provided in section 2 of Article X of these bylaws.

Whenever, in the opinion of the board of directors, the capital funds of the association are in excess of that amount necessary for its sound financial operation, the board of directors shall call for redemption, and redeem or retire, in accordance with section 3 of Article VII of the articles of incorporation, an amount of oldest outstanding preferred stock in the same order as originally issued, equal to the amount of such excess, provided that no stock shall be retired unless the stock outstanding thereafter shall at least equal 40 percent of the original cost of the fixed facilities and permanent additions thereto.

ARTICLE XII

Distribution of Assets on Liquidation

In the event of the dissolution or liquidation of the association, any assets remaining after the payment of all debts, insofar as they are sufficient for that purpose, shall be distributed in the following order and manner:

(1) All outstanding preferred stock and credits on preferred stock shall be retired in full.

(2) All outstanding common stock and credits on common stock shall be retired in full.

(3) Unexhausted interests of members and patrons in general reserves shall be retired ratably on an equitable basis, as determined by the board of directors.

(4) The remaining assets shall be distributed to the patrons of the association on as equitable a patronage basis as the board of directors finds practicable.

ARTICLE XIII

Fiscal Year

The fiscal year of the association shall begin on the first day of _____, and end on the last day of _____ of each year.

ARTICLE XIV

Seal

The seal of the association shall contain these words and figures: "_____ Association, Incorporated 19_____" in circular form, the impress of which is placed hereon.

ARTICLE XV

These bylaws may be altered or amended by a vote of the majority of the holders of fully paid-up common stock in good standing at any annual or special meeting of the stockholders at which a quorum is present, but notice of the proposed change shall be given in the notice of the meeting.

We, the undersigned, being all the incorporators and stockholders of the _____ Association, do hereby assent to the foregoing bylaws and adopt the same as the bylaws of said association.

IN TESTIMONY WHEREOF, we have set our hands this _____ day of _____, 19____.

COMMON STOCK CERTIFICATE

Incorporated in _____

No. _____

ONE SHARE

(Name of Association)

(Address)

AUTHORIZED CAPITAL \$ _____

COMMON STOCK: _____ Shares PREFERRED STOCK: _____ Shares

Par Value \$ _____ per share Par Value \$ _____ per share

This certifies that _____ is the owner of one share of common stock, of a par value of _____ Dollars (\$ _____) of _____

transferable on the books of the association on the surrender of this certificate, properly endorsed, by the holder thereof, or by attorney properly authorized, which stock is subject to the following conditions:

(Here insert sections 2 and 4 of Article VII of the articles of incorporation)

This certificate of common stock is subject to performance given to preferred stock in the articles of incorporation of the association, and the holder hereof accepts the same subject to such preference, and is also subject to all the other terms and conditions of the articles of incorporation and the bylaws now in effect or hereafter adopted.

IN WITNESS WHEREOF the said association has caused this certificate to be signed by its duly authorized officers and its corporate seal to be hereunto affixed.

This _____ day of _____, 19____.

Attest:

Secretary

President

TRANSFER OF COMMON STOCK

(To be printed on back of stock certificates)

For value received, and with consent of the board of directors, _____ hereby sell, assign and transfer unto _____ the shares of common stock represented by the within certificate, and do hereby irrevocably constitute and appoint _____ to transfer the said stock on the books of the within-named corporation with full power of substitution in the premises.

Dated _____, 19____.

In presence of:

Notice: The signature of this assignment must correspond with the name as written upon the face of the certificate in every particular without alteration or enlargement or any change whatever.

PREFERRED STOCK CERTIFICATE

Incorporated in _____

No. _____ Shares

Retirement Order.

No. _____

(Name of Association)

(Address)

AUTHORIZED CAPITAL \$ _____

COMMON STOCK: _____ Shares PREFERRED STOCK: _____ Shares

Par Value \$ _____ per share Par Value \$ _____ per share

This certifies that _____ is the owner
of _____ shares of preferred stock, of a par
value of _____ Dollars (\$ _____), each of _____

(Name of association)

(Town)

_____, transferable on the books of the
(State)
association on the surrender of this certificate, properly endorsed,
by holder thereof, or by an attorney properly authorized, which
stock is subject to the following conditions:

(Here insert sections 3 and 4 of Article VII of the articles
of incorporation)

IN WITNESS WHEREOF the said association has caused this cer-
tificate to be signed by its duly authorized officers and its cor-
porate seal to be hereunto affixed.

This _____ day of _____, 19____.

ATTEST:

Secretary

President

TRANSFER OF PREFERRED STOCK

(To be printed on back of stock certificates)

For value received _____ hereby sell, assign and transfer unto _____ shares of preferred stock represented by the within certificate, and do hereby irrevocably constitute and appoint _____ to transfer the said stock on the books of the within-named corporation with full power of substitution in the premises.

Dated _____, 19__.

In presence of:

Notice: The signature to this assignment must correspond with the name as written upon the face of the certificate in every particular without alteration or enlargement, or any change whatever.

WAIVER OF NOTICE OF FIRST MEETING

OF

STOCKHOLDERS

We, the undersigned, being all of the incorporators of the

_____, of _____, _____
(Name of Association) (Town) (State)

constituting all of the present stockholders of such association, hereby waive notice of a meeting of the stockholders and consent to the holding of a meeting of such stockholders at _____ o'clock ____ M.

on the _____ day of _____, 19__, at

_____ in _____, _____
(Place of meeting) (Town) (State)

for the purpose of adopting bylaws for the government of the association and transacting any other business that may properly come before the meeting.

WITNESS our signatures this _____ day of _____, 19__.

WAIVER OF NOTICE OF FIRST MEETING

OF

DIRECTORS

WE, the undersigned, being all of the directors of _____
(Name of

Association) _____, _____ (Town) _____, _____ (State)

hereby waive notice of a meeting of the directors and consent to the
holding of a meeting of such directors at _____ o'clock _____ M.

on _____ the _____ day of _____, 19__,
(Day)

at _____ in _____, _____
(Place of Meeting) (Town) (State)

for the purpose of electing officers of the association to serve dur-
ing the ensuing year, adopting the form of ginning agreement, and
transacting any other business that may properly come before said
meeting.

WITNESS our signatures this _____ day of _____, 19__.

MINUTES OF FIRST MEETING
OF
STOCKHOLDERS

The first meeting of the stockholders, consisting of the incorporators of _____ was held at _____ o'clock
(Name of association)
____ M. on the _____ day of _____, 19____, at
_____, in _____, _____.
(Place of meeting) (Town) (State)

The chair called for proof of notice of the meeting, whereupon _____ presented a waiver of notice and consent to hold the meeting signed by all of the stockholders of the association, which waiver and consent was in the following form:

(Copy waiver of notice and consent to meeting.)

The chair ruled that the meeting was properly called and it was ascertained that _____ stockholders of the association, constituting a quorum, were present. The chair reported that the articles of incorporation of the association were filed on the _____ day of _____, 19____, at _____ o'clock in the _____ noon, in the office of the Secretary of State of the State of _____, and presented a copy of said articles of incorporation, which was read, and on motion duly made, seconded and carried, was directed to be entered in full in the minute book. A draft of proposed bylaws for the government of the association was presented by _____ and was read to the meeting and discussed section by section and as a whole, and was unanimously adopted. Each stockholder affixed his signature to the bylaws and the secretary was instructed to spread the bylaws on the minutes of this meeting.

(Here insert record of any other business that may have been transacted.)

There being no further business to come before the meeting, on motion duly made, seconded and unanimously adopted, the meeting was adjourned.

(Temporary chairman)

(Temporary secretary)

MINUTES OF FIRST MEETING

OF

BOARD OF DIRECTORS

The first meeting of the board of directors of the _____
(Name of
Association) _____, _____ (Town) _____, _____ (State)
was held at _____ o'clock _____ M. on _____, _____
(Day)
_____, 19____, at _____, in _____,
(Place of meeting) (Town)
_____.
(State)

Upon convening, _____ was elected temporary
chairman and _____ temporary secretary of the
meeting, and each assumed his office.

The chair called for proof of notice of the meeting, whereupon
_____ presented a waiver of notice and con-
sent to holding the meeting, signed by all of the directors of the
association, which waiver and consent was as follows:

(Copy waiver of notice, and consent to holding meeting.)

Upon roll call of the directors of the association, the follow-
ing answered present:

(Record the names of all directors present.)

The chair ruled that proper and legal notice of the meeting had
been given and that a quorum was present, and announced that the
meeting was open for transacting business.

The chair stated that the meeting was called for the purpose of
electing officers of the association for the ensuing year and trans-
acting any other business that might properly come before the meeting.

Upon motion duly made and seconded, the following officers were
unanimously elected to serve at the discretion of the board until the
time of the first regular meeting of the board to be held as soon as
practicable following the first annual meeting of the stockholders:

(Record the names of the officers elected and the title
of office.)

Following the election of the officers, the president took the chair, and the secretary-treasurer assumed the duties as secretary of the meeting.

Upon motion duly made and seconded, the following resolution was adopted:

RESOLVED, that the president and secretary be and they are hereby authorized to have prepared and to issue certificates of stock in form as submitted to this meeting, and each in form as follows:

(Here insert form of certificate of common stock and form of certificate of preferred stock.)

Upon motion duly made and seconded, the following resolution was adopted:

RESOLVED, that the president and secretary be and they are hereby authorized to have printed a sufficient number of copies of the articles of incorporation and bylaws, so that a copy thereof may be delivered to each member, and each person who may later become a member of the association.

Upon motion duly made and seconded, the following resolution was adopted:

RESOLVED, that the ginning agreement, in form as submitted to this meeting, a copy of which appears hereafter, is hereby adopted:

(Here insert form of ginning agreement.)

Upon motion duly made and seconded, the following resolution was adopted:

RESOLVED, that all subscriptions for stock in the association appearing on the list submitted by the secretary, be accepted, and that the president and secretary be and they hereby are directed to enter into ginning agreements with all subscribers for common stock, and to carry out the terms and conditions thereof, and to solicit additional subscriptions for stock, and signatures to the ginning agreement, for submission to the board of directors for approval.

Upon motion duly made and seconded, the following resolution was adopted:

RESOLVED, that the _____ Bank be selected as a depository for the funds of the association.

Upon motion duly made and seconded, the following resolution was adopted:

RESOLVED, that all checks drawn upon the _____ Bank, for withdrawal of funds of the association on deposit there-with, be signed by the secretary-treasurer and countersigned by either the president or the vice president.

Upon motion duly made and seconded, the following resolution was adopted:

RESOLVED, that the secretary-treasurer is hereby authorized to receive all funds paid into the association, endorse all checks and other media of exchange, and deposit the same to the account of the association in _____ Bank.

Upon motion duly made and seconded, the following resolution was adopted:

RESOLVED, that the president and secretary be and they hereby are authorized and directed to obtain fidelity bond coverage in the amounts stated herein on the following officers, agents and employees as required by the bylaws; and that such bonds be submitted to the board of directors for approval at its next meeting.

<u>Name</u>	<u>Office</u>	<u>Amount of bond</u>
-------------	---------------	-----------------------

(Similar resolutions may be adopted, providing for the insurance of the property of the association, upon its acquisition, and for adequate insurance covering other liabilities, and authorizing the employment of a manager and other employees.)

There being no further business to come before the meeting, on motion duly made, seconded and unanimously adopted, the meeting adjourned.

Chairman

Secretary

APPENDIX B

In order for a cooperative association of producers to be exempt from the payment of Federal income taxes it must meet, and be operated in a manner consistent with, the terms and conditions of paragraph 12 of section 103 of the Federal Revenue Act of 1938, which reads as follows:

"(12) Farmers', fruit growers', or like associations organized and operated on a cooperative basis (a) for the purpose of marketing the products of members or other producers, and turning back to them the proceeds of the sales, less the necessary marketing expenses, on the basis of either the quantity or the value of the products furnished

by them, or (b) for the purpose of purchasing supplies and equipment for the use of members or other persons, and turning over such supplies and equipment to them at actual cost, plus necessary expenses. Exemption shall not be denied any such association because it has capital stock, if the dividend rate of such stock is fixed at not to exceed the legal rate of interest in the State of incorporation or 8 per centum per annum, whichever is greater, on the value of the consideration for which the stock was issued, and if substantially all such stock (other than nonvoting preferred stock, the owners of which are not entitled or permitted to participate, directly or indirectly, in the profits of the association, upon dissolution or otherwise, beyond the fixed dividends) is owned by producers who market their products or purchase their supplies and equipment through the association; nor shall exemption be denied any such association because there is accumulated and maintained by it a reserve required by State law or a reasonable reserve for any necessary purpose. Such an association may market the products of nonmembers in an amount the value of which does not exceed the value of the products marketed for members, and may purchase supplies and equipment for nonmembers in an amount the value of which does not exceed the value of the supplies and equipment purchased for members, provided the value of the purchases made for persons who are neither members nor producers does not exceed 15 per centum of the value of all its purchases. Business done for the United States or any of its agencies shall be disregarded in determining the right to exemption under this paragraph." (52 Stat. 480, Title 26 U.S.C. Sec. 103, paragraph 12.)

In order for a cooperative association of producers to be eligible to borrow from a bank for cooperatives, it must meet and be operated in a manner consistent with, the terms and conditions of section 15 of the Agricultural Marketing Act as amended, which reads as follows:

"* * * As used in this Act the term 'Cooperative Association' means any association in which farmers act together in processing, preparing for market, handling, and/or marketing the farm products of persons so engaged, and also means any association in which farmers act together in purchasing, testing, grading, processing, distributing, and/or furnishing farm supplies and/or farm business services: Provided, however, that such associations are operated for the mutual benefit of the members thereof as such producers or purchasers and conform to one or both of the following requirements:

First. That no member of the association is allowed more than one vote because of the amount of stock or membership capital he may own therein; and

Second. That the association does not pay dividends on stock or membership capital in excess of 8 per centum per annum. And in any case the following:

Third. That the association shall not deal in farm products, farm supplies, and farm business with or for nonmembers in an amount greater in value than the total amount of such business transacted by it with or for members. * * *" (46 Stat. 18; 48 Stat. 266; 49 Stat. 317 -- Title 12 U.S.C. Sec. 1141j.)

